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SUBJECT: Lai Appointment Agitates Taiwan Investors in South China

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¶1. (SBU) Summary: Ma Ying-jeou's appointment of the Taiwan Solidarity Union's (TSU) Lai Shin-yuan as chair of the Mainland Affairs Council (MAC) has been as lively a topic of interest, positive and negative, among Taiwan businessmen in the Pearl River Delta as in Taiwan. Close friends are divided. Chang Han-wen, chair of China's National Taiwan Business Association (TBA), sees the appointment as a betrayal of KMT supporters, while Andrew Yeh, Chair of the Dongguan (TBA), says Ma needs Lai to put the brakes on other KMT leaders (Lien Chan and Chiang Pin-kung) who might be tempted to move too fast on cross-Straits opening. Both business leaders look forward to the Straits Exchange Foundation (SEF) assuming an unofficial consular role in the mainland and providing assistance to Taiwan investors here. They lamented worsening business conditions in the Pearl River Delta for Taiwan firms and the difficult decisions investors face, whether to move elsewhere in China, move to Southeast Asia, stay put and monitor the situation, or close up shop and go home. They expect many factories to shut down and local industries to see consolidation. End Summary.

One Appointment, Different Interpretations

¶2. (SBU) With hardly a nudge on our part, except to ask what's the latest news's from Taiwan, south China's Taiwan business leaders launched into a conversation (sometimes among themselves rather than with us) about the appointment of the Taiwan Solidarity Union's Lai Shin-yuan as chair of the Mainland Affairs Council (MAC). While the chair of China's National Taiwan Business Association (TBA), Chang Han-wen, expressed profound disappointment, Andrew Yeh, the chair of the Dongguan Taiwan Business Association (China's largest), said he was optimistic that Lai's appointment would not impede progress on further opening of cross-Straits economic relations.

¶3. (SBU) Chang, who owns a shoe factory in Dongguan and a couple of hotels in Shanghai and who has chaired the National TBA since it was founded in April 2007, criticized Ma for trying to please Taiwan's green party members instead of the seven million voters who supported him in the March 22 elections. (Note: according to Chang, some 30,000 Taiwans from Dongguan had returned to Taiwan to vote for Ma - a startling and seemingly inflated figure. End note.) Chang told the Consul General that Kuomintang (KMT) Vice Chair Chiang Pin-kung had been with him when a Taiwan reporter called Chang to ask for comment on Lai's appointment. He said Chiang, was startled, having not been apprised earlier of Lai's appointment. Chang expects the appointment to make cross-Straits cooperation more difficult and possibly delay the implementation of weekend charter flights anticipated to begin on July 4.

14. (SBU) Chang, who met Lai during a recent trip to Taipei, told us that she said as a member of Ma's administration she would follow a "one China" policy. Chang was not entirely surprised that Ma chose to appoint a figure like Lai to head the MAC, commenting that Ma needed to demonstrate to green voters that he would not betray Taiwan. He compared the appointment to Ma's decision to name Vincent Siew as his running mate, noting that many deep-blue KMT members dislike Siew.

15. (SBU) Andrew Yeh, the chair of Dongguan's TBA, called Lai's appointment a practical move by Ma to balance power among internal KMT factions. Ma, he said, needed to appoint Lai to check the influence of older KMT politicians who have been active in developing informal cross-strait ties, especially Honorary Chair Lien Chan and Chiang Pin-kung. He compared Lai to the brakes on a car that might otherwise go out of control. In Yeh's view, Lien's trip to China after the KMT victory - and without notification of the president elect - had not been respectful. If Lai can restrain Lien, Ma will have nothing to fear from others in the KMT who might challenge his authority. Yeh noted that Lai had already shown that she had the right personality to play bad cop for Ma. However, even though he agrees with the strategy, he believes that Lai was not the right choice; her ethics and loyalty are clearly an issue.

16. (SBU) Both Chang and Yeh emphasized that Ma will move cautiously on cross-strait relations. Chang explained that Ma prefers the status quo as do Taiwan investors in the mainland. Yeh commented that Ma would not want to move too fast on cross-strait opening in order to make sure he keeps some bargaining chips with Beijing.

Great Expectations for the Straits Exchange Foundation

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17. (SBU) The two business leaders are hopeful that the Straits Exchange Foundation (SEF) will take an active role in assisting Taiwan investors in China. They anticipate that the SEF offices in China would be able to act as unofficial consulates. Chang explained that investors now look to the TBAs to play that role, but with no official power the associations must rely on their connections to help investors resolve disputes. Yeh believes that the semi-official status of SEF offices would make a big difference in protecting the interests of Taiwan businesses.

18. (SBU) Chang expressed surprise that Ma had not appointed the KMT's Chang Rong-gong, who had worked closely with Chiang Pin-kung on cross-strait issues, to be secretary general of the SEF. Chang Han-wen attributed Ma's decision to appoint Chang Rong-gong to be deputy secretary general of the KMT instead to Ma's desire to limit Chiang's control of SEF.

Dongguan's Economic Prospects Dim

19. (SBU) The investment environment for Taiwan firms in the Pearl River Delta, and especially in Dongguan, is deteriorating substantially, according both Chang and Yeh. Chang noted that the number of Taiwan enterprises in Dongguan had fallen from 6,500 to 5,000 recently due to rising costs and new government policies, namely the new Labor Contract Law, and new regulations governing export processing industries. Yeh also highlighted the impact of renminbi (RMB) appreciation vis-a-vis the dollar, economic weakening in the United States due to the sub-prime mortgage crisis, and labor and energy shortages in the Pearl River Delta.

110. (SBU) Chang argued that the Labor Contract Law has had the strongest impact on Taiwan investors. He supports protection of workers' rights but pointed out that the law's details had not been spelled out. According to Chang, unscrupulous attorneys have exaggerated the protections offered to workers by the law, for example telling them that they could get back overtime pay. As a result, workers in many area factories had gone on strike. Chang said workers in a factory just across the street and another nearby had gone on strike three days ago. A month ago, a factory owned by the previous Dongguan TBA chair had been hit by a strike, and Taiwan

media had reported that employees in another factory had rioted. However, Chang acknowledged that firms that had already strictly observed labor regulations, such as contract manufacturers for major international brands that were subject to regular inspections, had not seen much impact from the new law. Yeh commented that firms in the Yangzi River Delta area, where the rule of law was somewhat stronger, had been less affected by the new law because the labor market was more tightly regulated there.

¶11. (SBU) Chang also told us that a recent rumor about plans to reduce the population of Dongguan had disturbed Taiwan investors. According to the rumor, Guangdong Party Secretary Wang Yang had visited Dongguan and told Liu Zhigeng, the city's party secretary, that the per capita value-added output was too low. Wang instructed Liu to reduce the Dongguan population by half. Chang observed that many Taiwan firms would not be able to survive without Dongguan's large migrant labor population.

Headed Toward Consolidation

¶12. (SBU) The Chinese government aims to encourage labor-intensive firms in the Pearl River Delta region to move to other less developed parts of China, like Hunan and Jiangxi. This will be difficult for Taiwan firms, according to Chang, who took note of relocation costs, increased transportation time and other expenses associated with inland areas. In addition, investors fear that investment incentives and other favorable policies in these less developed areas won't last long.

¶13. (SBU) Some firms are moving to Southeast Asian countries like Vietnam, Cambodia or Indonesia. Yeh pointed out that investing in Vietnam was not really a viable solution for the export-processing industry's problems. He argued that if a country of 1.3 billion couldn't provide an adequate labor pool, then a county of 80 million would certainly be unable as well.

¶14. (SBU) Some firms, like Chang's, are staying put and watching the situation; others are closing down. Chang said that even some of Dongguan's younger Taiwan investors are now more than 50 years old, and if the situation deteriorates, he predicts many of them will shut down their factories and return home. Yeh foresees consolidation in the industry. Survivors will gain market share, but the price of finished products will rise.

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High-Tech Development Faces Challenges

¶15. (SBU) Chang is not optimistic about the Pearl River Delta's potential to cultivate high-tech industries to replace labor-intensive ones forced out by changing conditions. He noted that the Dongguan government had poured investment into the Songshan Lake High-Tech Park but had seen little success in attracting tenants. High-tech industries rely on highly skilled workers, and Chang pointed out that those workers would prefer to live in eastern China, especially Shanghai. The future was not particularly bright, Chang said, pointing to the fate of manufacturing cities in the United States that have struggled to transform.

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